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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact: , ID No.

Telephone Number:

Refer Reply To:
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Re:

Legend

Grantor	=
Son	=
Spouse	=
Child 1	=
Child 2	=
Child 3	=
Trust	=

Trust 1	=
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Date 1	=
Date 2	=
Date 3	=
Date 4	=
Date 5	=
Date 6	=
Date 7	=
Court 1	=

Court 2	=
State 1	=
State 1 Statute	=
State 2	=

Dear

This letter responds to your authorized representative's letter of March 5, 2013 requesting rulings on the gift, estate, generation-skipping transfer (GST), and income tax consequences of proposed modifications and division of a trust.

Facts

The facts and representations submitted are summarized as follows: Grantor established a revocable trust (Trust) on Date 1. Trust was amended on Date 2.

Trust, as amended, provides that upon Grantor's death, trustees shall divide all of the assets of the trust into as many equal shares as there are children of Grantor then living or who, if deceased, have a wife or descendants then living, with each share to be held as a separate trust designated by the name of the beneficiary for whom the separate share was created.

Grantor died on Date 3. Trustees then divided Trust and created a separate trust (Trust 1) for the benefit of Son. No further contributions were made to Trust after Date 3. Date 3 is prior to September 25, 1985.

On Date 4, Court 1 entered an order changing the corporate trustee for Trust 1. On Date 5, Court 1 entered an order changing the corporate trustee for Trust 1 and transferred the situs of Trust 1 to State 2. However, State 1 law continues to govern the validity and construction of the trust.

On Date 6, Court 2 entered an order approving the resignation of the corporate co-trustee, confirming the appointment of a successor corporate co-trustee, accepting jurisdiction over Trust 1, reforming Trust 1 to create a position of Investment Advisor and appoint Son as the Initial Investment Advisor and to give the individual trustees the power to remove and replace the corporate trustees.

Article IV, paragraph A.1. of Trust 1 provides that the Trustees in their discretion may pay and distribute all or part of the income of the trust to or for the benefit of Son, Son's spouse (Spouse), or any one or more of Son's descendants in monthly or other convenient installments, and also provides that the trustee must accumulate any undistributed trust income and add it to trust principal. Article IV, paragraph A.2. provides that the trustees in their discretion may make distributions of principal to or for the benefit of any income beneficiary of the trust for any purpose the trustees consider to be worthwhile and in the best interest of that income beneficiary, including maintenance, care, support, and other worthwhile purposes. Article IV, paragraph A.3. provides that the trustees in their discretion may make distributions of income or principal of the trust to qualifying charitable organizations.

Article IV, paragraph A provides that any time after Son's death that he has no living child who is less than 21 years old and no living wife who has not remarried, the trustees must divide the remaining principal and undistributed income of the trust into as many equal shares as there are children of Son, who are then living or who if deceased have issue then living, with each share to be held as a separate trust designated by the name of the grandchild of Grantor for whom the separate trust is created. Article IV, Paragraph B.3. provides that if after the death of a grandchild of Grantor there is no living child of grandchild who is less than 21, the trustees will pay and distribute all of the remaining principal and undistributed income to the then living issue of such grandchild by right of representation.

Article VII, paragraph A.13. provides that the trustee has the power, to divide the trust or make a distribution from the trust, in whole or in part, or in kind, and the decision of the trustees as to the value of any asset thereof or the composition of such share, shall be conclusive if reached with reasonable care.

Son is currently married to Spouse. Son has three adult children, Child 1, Child 2, and Child 3. Child 1 does not have any children. Child 2 and Child 3 each have one child, both minors. Each family line has different investment philosophies regarding asset allocation, passive versus active investment management, and use of alternative investments. This led to a desire to invest the trust assets differently among the children's shares. The trustees believe this can be best accomplished through a division of Trust 1 into "Successor Trusts." The modifications and division of Trust 1 in this manner will allow each separate Successor Trust to be managed and invested according to the best interests Child 1, Child 2 and Child 3. The dispositive terms of each Successor Trust will be substantially the same as the dispositive terms of Trust 1.

On Date 7, the individual trustees and current beneficiaries of Trust 1 filed a petition with Court 2 requesting division of the trust property on a pro rata basis into three separate and distinct shares: one for Son, Spouse, Child 1, Child 1's descendants and charitable organizations; one for Son, Spouse, Child 2, Child 2's descendants, and charitable organizations; and one for Son, Spouse, Child 3 and Child 3's descendants, and charitable organizations. Each separate and distinct trust would be administered according to the terms and conditions of Trust 1, as modified by Court 2. The Attorney General was provided a copy of the petition and did not oppose the relief requested in the petition.

State 1 Statute provides that a trustee may, without approval of any court, divide a trust before or after it is funded, into two or more separate trusts if the trustee determines that dividing the trust is in the best interest of all persons interested in the trust and will not substantially impair the accomplishment of the purposes of the trust.

You have requested the following rulings:

1. The modifications and division of Trust 1 into Successor Trusts will not alter the inclusion ratio of Trust 1 or the Successor Trusts for GST tax purposes.
2. The modifications and division of Trust 1 into Successor Trusts will not create a transfer of property subject to federal gift tax under § 2501 of the Internal Revenue Code.
3. The modifications and division of Trust 1 into Successor Trusts will not cause any portion of the assets of Trust 1 or the Successor Trusts to be includible in the gross estate of any beneficiary under §§ 2035, 2036, 2037, or 2038.
4. The Successor Trusts will be treated as separate taxpayers for federal income tax purposes pursuant to § 643(f).
5. The modifications and division of Trust 1 into Successor Trusts will not result in treating any Trust 1 property as paid, credited, or distributed for purposes of § 661 or § 1.661(a)-2(f) of the Income Tax Regulations, and so will not result in realization of any income, gain, or loss under § 661 or 662 by Trust 1, the Successor Trusts, or a beneficiary of any of the trusts. In addition, the modifications and division of Trust 1 into Successor Trusts will not result in the realization of any income, gain or loss to Trust 1, the Successor Trusts, or a beneficiary of any of those trusts under § 61 or § 1001.
6. The modifications and division of Trust 1 into Successor Trusts will result in each Successor Trust holding its share of Trust 1's property with the same basis as it had when owned by Trust 1 at the time of the division into Successor Trusts under § 1015.

Ruling 1

Section 2601 imposes a tax on each generation-skipping transfer. Section 2611(a) provides that the term "generation-skipping transfer" means a taxable distribution, a taxable termination, and a direct skip.

Section 1433(b)(2)(A) of the Tax Reform Act of 1986 and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations provide that the generation-skipping transfer tax shall not apply to any generation-skipping transfer under a trust that was irrevocable on September 25, 1985, but only to the extent that such transfer is not made out of corpus added to the trust after September 25, 1985 (or out of income attributable to corpus so added).

Section 26.2601-1(b)(1)(ii)(A) provides that any trust in existence on September 25, 1985, will be considered an irrevocable trust except as provided in § 26.2601-1(b)(1)(ii)(B) or (C) (relating to property includible in the grantor's gross estate under §§ 2038 and 2042).

Section 26.2601-1(b)(4)(i) provides rules for determining when a modification, judicial construction, settlement agreement, or trustee action with respect to a trust that is exempt from the generation-skipping transfer tax will not cause the trust to lose its exempt status. The regulation provides that the rules contained in the paragraph are applicable only for purposes of determining whether an exempt trust retains its exempt status for generation-skipping transfer tax purposes. The rules do not apply in determining, for example, whether the transaction results in a gift subject to gift tax, or may cause the trust to be included in the gross estate of a beneficiary, or may result in the realization of capital gain for purposes of § 1001.

Section 26.2601-1(b)(4)(i)(D) provides that a modification of the governing instrument of an exempt trust (including a trustee distribution, settlement, or construction that does not satisfy paragraph (b)(4)(i)(A), (B), or (C) of this section) by judicial reformation, or nonjudicial reformation that is valid under applicable state law, will not cause an exempt trust to be subject to the provisions of chapter 13, but only if --

(1) The modification does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation (as defined in § 2651) than the person or persons who held the beneficial interest prior to the modification, and

(2) The modification does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust.

In this case, Trust 1 was created and irrevocable before September 25, 1985. It is represented that no additions have been made to Trust 1 since September 25, 1985. Consequently, Trust 1 is currently exempt from GST tax.

The proposed modifications and division of Trust 1 will result in three trusts, one each for the benefit of Son, Spouse, and each of Son's children and their issue. The dispositive terms of each Successor Trust will be substantially the same as the dispositive terms of Trust 1, although limited to a particular family line. Each resulting trust will terminate no later than the original termination date of Trust 1. Accordingly, the proposed modifications and division of Trust 1 into the Successor Trusts will not shift a beneficial interest to any beneficiary who occupies a lower generation than the person or persons who held the beneficial interest prior to the modifications and division, and will not extend the time for the vesting of any beneficial interest in a Successor Trusts beyond the period provided for in Trust 1.

Accordingly, based on the facts submitted and the representations made, and provided that Court 2 issues an order approving the modifications and division of

Trust 1, the modifications and division of Trust 1 into Successor Trusts will not alter the inclusion ratio of Trust 1 or the Successor Trusts for GST tax purposes.

Ruling 2

Section 2501 imposes a tax for each calendar year on the transfer of property by gift during such calendar year by any individual.

Section 2511(a) provides that the gift tax applies whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property transferred is real or personal, tangible or intangible.

In this case, Trust 1 will be divided into three Successor Trusts. Each Successor Trust will benefit Son, Spouse, one of Son's children, their issue, and charities. The dispositive provisions of each Successor Trust will be substantially the same as the dispositive provisions of Trust 1. Each resulting trust will terminate no later than the date on which Trust 1 terminates.

Based on the facts submitted and the representations made, and assuming the transaction is carried out as proposed and is effective under state law, we conclude that the modifications and division of Trust 1 into Successor Trusts will not create a transfer of property subject to federal gift tax under § 2501.

Ruling 3

Section 2033 provides that the value of the gross estate includes the value of all property to the extent of the interest therein of the decedent at the time of his death.

Section 2035(a) provides that if (1) the decedent transferred an interest in property or relinquished a power with respect to any property, during the 3-year period ending on the date of the decedent's death, and (2) the value of the property (or interest therein) would have been included in the gross estate under § 2036, 2037, 2038, or 2042 if the interest or power had been retained by the decedent on the date of death, then the value of the gross estate shall include the value of any property (or interest therein) that would have been so included. Under § 2035(b), the gross estate shall be increased by the amount of any gift tax paid by the decedent or his estate on any gift made by the decedent or his spouse during the 3-year period ending on the date of decedent's death.

Section 2036(a) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate consideration in money or money's worth), by trust or otherwise, under which the decedent has retained for his life or for any period not ascertainable without reference to the decedent's death or for any period which does not in fact end before the decedent's

death - (1) the possession or enjoyment of, or the right to the income from, the property, or (2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom.

Section 2037(a) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, if (1) the possession or enjoyment thereof can, through ownership of such interest, be obtained only by surviving the decedent, and (2) the decedent has retained a reversionary interest in the property and the value of the reversionary interest immediately before the death of the decedent exceeds 5 percent of the value of the property.

Section 2038(a)(1) provides that the value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, where the enjoyment thereof was subject at the date of the decedent's death to any change through the exercise of a power (in whatever capacity exercisable) by the decedent alone or by the decedent in conjunction with any other person (without regard to when or from what source the decedent acquired such power), to alter, amend, revoke, or terminate, or where any such power is relinquished during the 3-year period ending on the date of the decedent's death.

In order for §§ 2035 through 2038 to apply, a decedent must have made a transfer of property or any interest therein (except in the case of a bona fide sale for an adequate and full consideration in money or money's worth) under which the decedent retained an interest in, or power over, the income or corpus of the transferred property.

Based on the facts submitted and the representations made, we conclude that the proposed modifications and division of Trust 1 do not constitute a transfer by any beneficiary within the meaning of §§ 2035 through 2038. The beneficiaries of the Successor Trusts have the same interests after the modifications and division as they had prior to the modifications and division. Therefore, nothing will be transferred by them by reason of the proposed modifications and division. Accordingly, based upon the facts submitted and the representations made, we conclude that the modifications and division of Trust 1 into Successor Trusts will not cause any portion of the assets of Trust 1 or the Successor Trusts to be includible in the gross estate of any beneficiary under §§ 2035, 2036, 2037, or 2038.

Ruling 4

Section 643(f) provides that, for purposes of Subchapter J of Chapter 1 of Subtitle A, under regulations prescribed by the Secretary, two or more trusts shall be treated as one trust if (1) such trusts have substantially the same grantor or grantors and substantially the same primary beneficiary or beneficiaries, and (2) a principal purpose of such trusts is the avoidance of the tax imposed by Chapter 1.

Section 1806(b) of the Tax Reform Act of 1986 provides that § 643(f) shall apply to taxable years beginning after March 1, 1984; except that, in the case of a trust that was irrevocable on March 1, 1984, it shall apply only to that portion of the trust that is attributable to contributions of corpus after March 1, 1984.

The trustees represent that each Successor Trust will have different beneficiaries. The trustees also represent that no portion of the principal of Trust 1 was contributed after March 1, 1984. Based on the facts submitted and the representations made, we conclude that as long as the Successor Trusts are separately managed and administered, they will be treated as separate trusts for federal income tax purposes.

Ruling 5

Section 661(a) provides that in any taxable year a deduction is allowed in computing the taxable income of a trust (other than a trust to which subpart B applies), for the sum of (1) the amount of income for such taxable year required to be distributed currently; and (2) any other amounts properly paid or credited or required to be distributed for such taxable year.

Section 1.661(a)-2(f) of the Income Tax Regulations provides that gain or loss is realized by the trust or estate (or the other beneficiaries) by reason of a distribution of property in kind if the distribution is in satisfaction of a right to receive a distribution of a specific dollar amount, of specific property other than that distributed, or of income as defined under § 643(b) and the applicable regulations, if income is required to be distributed currently.

Section 662 provides that there shall be included in the gross income of a beneficiary to whom an amount specified in § 661(a) is paid, credited, or required to be distributed (by an estate or trust described in § 661), the sum of the following amounts: (1) the amount of income for the taxable year required to be distributed currently to such beneficiary, whether distributed or not; and (2) all other amounts properly paid, credited, or required to be distributed to such beneficiary for the taxable year.

Based on the facts submitted and representations made, we conclude that the division of Trust 1 to create the three separate Successor Trusts is not a distribution under § 661 or § 1.661(a)-2(f).

Section 61(a)(3) provides that gross income includes gain derived from dealings in property.

Section 1001(a) provides that the gain from the sale or other disposition of property is the excess of the amount realized over the adjusted basis provided in § 1011 for determining gain, and the loss is the excess of the adjusted basis provided in § 1011 for determining loss over the amount realized. Under § 1001(c), the entire amount of gain or loss must be recognized, except as otherwise provided.

Section 1.1001-1(a) provides that, except as otherwise provided in subtitle A, the gain or loss realized from the exchange of property for cash or for other property differing materially either in kind or in extent is treated as income or loss sustained. Properties exchanged are materially different for purposes of § 1001(a) if the properties embody legal entitlements “different in kind or extent” or if the properties confer “different legal rights and powers.” *Cottage Savings Ass’n v. Comm’r*, 499 U.S. 554, 565 (1991). In *Cottage Savings*, the Court held that mortgage loans made to different obligors and secured by different homes embody distinct legal entitlements and that the taxpayer realized losses when it exchanged interests in the loans. *Id.* at 566.

Section 1.1001-1(h)(1) provides the severance of a trust is not an exchange of property for other property differing materially in kind or extent if: (i) an applicable state statute or the governing instrument authorizes or directs the trustee to sever the trust; and (ii) any non-pro rata funding of the separate trusts resulting from the severance, whether mandatory or in the discretion of the trustee, is authorized by an applicable state statute or the governing instrument.

Rev. Rul. 56-437, 1956-2 C.B. 507, concluded that the partition of a joint tenancy in which co-owners of property sever their interests is not a sale or exchange.

In this case, Trust 1’s assets will be distributed equally among the three Successor Trusts for the benefit of Child 1, Child 2, and Child 3. Each new trust contains an equal share of the assets of Trust 1. In addition, each Successor Trust retains a child of Son as a beneficiary. State 1 Statute authorizes the trustees to divide Trust 1; and (ii) any non-pro rata funding of the Successor Trusts resulting from the modifications and division, whether mandatory or in the discretion of the trustee, is authorized by the governing instrument. Accordingly, based upon the facts submitted and the representations made, we conclude that the proposed modifications and division of Trust 1 will not result in the realization of gain or loss under §§ 61 and 1001.

Ruling 6

Section 1015(a) provides that if the property was acquired by gift, the basis shall be the same as it would be in the hands of the donor or the last preceding owner by whom it was not acquired by gift, except that if the basis (adjusted for the period before the date of the gift as provided in § 1016) is greater than the fair market value of the property at the time of the gift, then for the purpose of determining loss the basis shall be the fair market value.

Section 1015(b) provides that if property is acquired after December 31, 1920, by a transfer in trust (other than by a transfer in trust by a gift, bequest, or devise), the basis shall be the same as it would be in the hands of the grantor increased in the amount of gain or decreased in the amount of loss recognized by the grantor on such transfer.

Section 1.1015-2(a)(1) provides that in the case of property acquired after December 31, 1920, by transfer in trust (other than by a transfer in trust by gift, bequest, or devise) the basis of property so acquired is the same as it would be in the hands of the grantor increased in the amount of gain or decreased in the amount of loss recognized to the grantor on the transfer under the law applicable to the year in which the transfer was made. If the taxpayer acquired the property by a transfer in trust, this basis applies whether the property be in the hands of the trustee, or the beneficiary, and whether acquired prior to termination of the trust and distribution of the property, or thereafter.

Based upon the facts submitted and representations made, we conclude that because § 1001 does not apply to the division of the trust assets, under § 1015 the basis of the trust assets will be the same after the modifications and division of Trust 1 as the basis of those assets before the modifications and division.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party.

Except as specifically ruled herein, we express or imply no opinion on the federal tax consequences of the transaction under the cited provisions or under any other provisions of the Code.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely,

Lorraine E. Gardner, Senior Counsel
Branch 4
Office of Associate Chief Counsel
(Passthroughs & Special Industries)

Enclosures
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